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A USER'S GUIDE TO FISCAL OVERSIGHT: A Toolkit for Charter School Authorizers





The National Charter School Resource Center (NCSRC) is dedicated to supporting the development of high-quality charter schools. The NCSRC provides technical assistance to sector stakeholders and has a comprehensive collection of online resources addressing the challenges charter schools face. The website hosts reports, webinars, and newsletters focusing on facilities, funding opportunities, authorizing, English learners, special education, military families, board governance, and other topics. The NCSRC is funded by the U.S. Department of Education and led by education consulting firm Safal Partners.

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INTRODUCTION



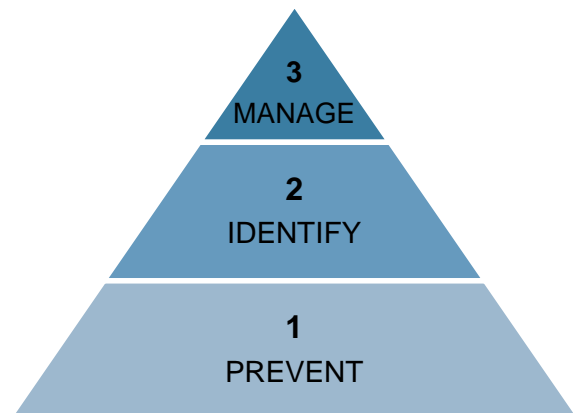
Purpose and Use of this Toolkit

The purpose of this toolkit is to equip charter school authorizers to exercise proper fiscal oversight. When charter schools close, it is generally due to a mix of financial, operational, and academic problems. Poor financial performance is often the most important factor in many closures.

This toolkit compiles best practices and recommendations based on a comprehensive literature review and interviews with subject matter experts, including authorizers, charter support organizations (CSOs), charter management organizations (CMOs), funders, attorneys, and charter finance specialists. The toolkit also draws from established findings on fraud and governance from the broader nonprofit sector.

Each subsection of this toolkit contains a set of checklists examining how to: 1) prevent, 2) identify, and 3) manage common financial issues. Of these, schools should aim first to prevent financial problems. However, the level of oversight and the complexity of each school's financial oversight system will depend on its specific needs. In some cases, detection and prevention may be the same since effective detection can deter potential fraud. Other stakeholders, such as school leaders and developers, can use the sections on 'prevention' to uncover potential school-level vulnerabilities.

Figure 1. Toolkit Framework



While the toolkit includes best practices, because specific needs depend on individual and state contexts, authorizers who use this toolkit should also be sure to consult their state law and legal counsel, as appropriate, to determine appropriate oversight.

Scope of Fiscal Responsibility

Both authorizers and governing boards are key stakeholders responsible for ensuring a school* is financially viable and able to pursue its primary educational goals. While some responsibilities of the board and the authorizer overlap, the activities of one do not reduce or replace the other's responsibilities, as each has different information about the school. To effectively oversee charter schools, authorizers must understand what constitutes strong financial oversight practices by schools. Likewise, the governing boards of schools need to understand what their authorizer expects and will do to oversee their school's financial operations. Please see the accompanying [Board Fiscal Oversight Toolkit](#) for more information.

Authorizers

Authorizers provide a layer of public accountability over the board and the school. Authorizers are ultimately responsible for the fiscal oversight of each charter school they oversee. Effective authorizing practices are essential, as charter closure rates due to fraud are overrepresented in states with weak charter authorizer laws.¹ During each phase of a charter school's life cycle, authorizers perform oversight tasks designed to ensure fiscal health – from application approval to oversight and monitoring to closure or renewal.

Authorizers primarily rely on school 'outputs' for information, such as produced reports, board-approved budgets, independent audits, and other documentation. Authorizers also perform direct oversight actions such as compliance monitoring and reviews of school performance, including site visits and interviews with staff and board members. It is important for authorizers to determine applicable state law requirements, including annual audits, budget projections, and quarterly financial statements.² Authorizers also vary by state in legal status, capacity, and access to funding. Some authorizers are traditional local educational agencies (LEA), while some are state education departments, universities, statewide independent charter boards, or other entities; therefore, each authorizer must identify the most appropriate recommendations to implement in the context of their structure and practices.

* When we refer to a "school," we are referring to the non-profit organization that holds the charter. However, there are exceptions to the non-profit structure. For example, in California, some charters are structured as public schools under California law. In Arizona, an individual may hold a charter contract. In most circumstances, a charter is held by a non-profit organization overseen by that school's governing board.

Types of Financial Issues

There are two major areas that cause financial issues for charter schools: financial insolvency and fraud. This toolkit distinguishes poor financial performance from fraud because the oversight practices and recommendations differ for each.

1. Lack of Financial Health and Sustainability

While cases of fraud may receive more attention, poor financial management is more common than financial misfeasance or fraud.³ The financial health and sustainability of a school require effective financial management by the school's board and leadership to establish the viability of the school. The Center for Education Reform identifies the two major drivers of financial failure for charter schools:⁴

- **Underenrollment**: Failing to attract enough students constrains the school's main source of revenue since public funding is tied directly to enrollment. Schools that over-estimate enrollment may suffer from underlying quality issues. Under enrollment is further complicated when schools fail to adjust budgets and expenditures, especially if enrollment drops during the school year.
- **Inadequate funding**: In many states, charter schools are considered their own district or LEA. This can create financial obligations for individual charter schools that most individual district-managed schools do not face. Regardless of LEA-status under each state's charter law, charter schools generally receive fewer dollars than the local traditional district schools.⁵ In particular, charter schools do not receive facilities funding in most states; they must spend operating funds on facilities costs, which constrains their operating budget. External risks, such as declines in charter school funding, exacerbate this issue and increase the probability of deficit and default. Depending on location, inadequate funding for specialized populations, such as students with disabilities and English learners, increases the challenge.

Other common issues that charter schools face include:

- A lack of financial expertise among the board or management;
- Facility-related issues, including insufficient equity, unsustainably high rent, and poor lease terms;
- Cash flow challenges related to delays in per pupil payments;
- Failure to properly anticipate and cover funding gaps; and
- Inadequate fundraising or unrealistic fundraising expectations.

2. Fraud and Misfeasance

Fraud is defined as deceiving or misrepresenting or as the crime of using dishonest methods to take something valuable.⁶ While it may ultimately lead to financial distress, fraud is distinct from poor financial management because it includes the underlying intent to deceive or misrepresent.⁷ Most relevant for this toolkit, it often takes the form of financial misfeasance or malfeasance¹. Some prior cases of charter school fraud have included:

- Asset misappropriation, including fraudulent check disbursements or expense reimbursements;
- Conflict of interest in procurement of services or facilities, such as related party transactions or self-dealing;
- Management companies that fail to deliver contracted services; and
- Inflation of enrollment figures and falsified attendance records.

It is impossible to eliminate the risk of fraud or mismanagement, and collusion increases the difficulty of detection, especially when school leaders or board trustees collude to manipulate documentation and reporting. However, the authorizer can mandate policies that ensure strong internal controls and a properly-implemented checks and balances system are in place to mitigate this risk. At the school level, the board must determine the most appropriate prevention and detection measures. Depending on circumstances, an authorizer can also encourage a board to perform a cost-benefit analysis to help identify weak points and policies to mitigate the greatest risks.

¹ Malfeasance is any intentional conduct that is wrongful or unlawful and is at a higher level of wrongdoing than nonfeasance (failure to act where there was a duty to act) or misfeasance (conduct that is lawful but inappropriate).

FINANCIAL OVERSIGHT: HEALTH AND SUSTAINABILITY



Prevention

While schools cannot anticipate every threat, proper planning and budgeting will strengthen a school's resilience to internal and external risks. Proper stewardship of public funds is primarily contingent on financial literacy, budgeting, monitoring, and risk management. By focusing on preventative measures, schools and authorizers can take a proactive approach to financial management.

1. ENSURE FINANCIAL LITERACY

- ☐ *Interview the founding board during the application stage and examine the collective years of board member financial experience.*
Authorizers should ensure that there is sufficient financial expertise and understanding on the board to execute the board's fiduciary duties.
- ☐ *Ensure authorizer financial capacity.*
Authorizers should ensure financial expertise within their own staffs and among external experts that review charter applications.

2. PROPER BUDGETING AND FORECASTS

- ☐ *Approve a conservative budget.*
Charter schools should budget conservatively. In particular, schools should estimate per pupil funding and fundraising carefully. Per pupil funding projections should be based on the last two years of expenditure by district and state charter school law funding provisions.⁸ Consider the current fiscal and funding environment and encourage the board to make adjustments accordingly. To prevent overreliance on a nonguaranteed funding source, authorizers should ensure that fundraising assumptions are at minimal amounts unless the school has already received written donor commitments.
- ☐ *Approve a long-term financial plan.*
The long-term financial plan is usually a 5-year budget for assumed per pupil revenues, capital projects, and operating expenses. Authorizers can require a revised budget if material changes occur, such as a large drop or increase in student enrollment.⁹
- ☐ *Benchmark the school's budget and expenses to comparable schools.*

Research per pupil expenses for charter schools in similar settings. Understand how the school's expenses differ from other schools because of a specific situation or mission (e.g. a focus on special education).¹⁰

☐ *Ensure a sufficient cash reserve balance is maintained.*

A commonly recommended target across experts and those we interviewed is about 5-10%¹¹ of the budget. Retaining excessive funds in reserve can also be perceived as evidence a school is not using per pupil funds as intended (i.e., on students). If cash reserves exceed 10% of the budget, check that the board has a plan to spend down excess reserves unless the large reserve is part of an appropriate long-term strategy, such as a facilities purchase or major upgrade.

3. REGULAR MONITORING PRACTICES

☐ *Review interim financial reports on a cash and accrual basis.*

Authorizers should review reports at least quarterly, with monthly reviews for high-risk schools, as determined by the authorizer's financial performance framework (see the following section, Identification, for more information). Ensure that the charter board is regularly reviewing the financial reports. Financial reports include the statement of activities (income statement), budget status report (budget vs. actual), statement of financial position (balance sheet), cash flow projections, enrollment (forecast vs. actual), and annual debt schedule if applicable. (*Discussed in further detail in the Identification section.*)

☐ *Establish clear expectations of monitoring and reporting with the school.*

Negotiate a clear charter contract or, in some states, a Memorandum of Understanding outlining school and authorizer responsibilities, such as frequency of site visits, financial reporting requirements, insurance coverage requirements, annual or semiannual reports for the authorizer, and any other required documentation.¹² Authorizers should clearly communicate any changes in timing or documentation requirements.

☐ *Consider audit findings in monitoring and intervention policies and practices.*

Because the financial performance review is based on self-reported information, unless specified in state law, authorizers should request independent auditor opinions across financial statements (including the balance sheet, income statement, and statement of cash flows)* to verify that they are accurate and complete. Authorizers can also receive guidance from auditors on the reporting methods used by the school.¹³

* The names of the financial statements differ according to whether the organization is for-profit, nonprofit, or governmental. The corresponding nonprofit names follow in parentheses: balance sheet (statement of financial position) and income statement (statement of activities and changes in net assets).

Identification

The National Association of Charter School Authorizers (NACSA) Financial Performance Framework is a core framework of financial monitoring primarily for authorizers. Authorizers may choose to use different ratios or calculations, but proper oversight should include indicators for school revenues, liquidity, and debt. The checklist below is a simplified version of the NACSA Financial Performance Framework with additional factors that may be red flags. The detailed Framework with measures and specific criteria is in Appendix A.

Using the Checklist

NACSA's performance framework categorizes the checklist into 'near-term' and 'sustainability' measures. Failing 'near-term' standards will show that the school is in immediate financial distress, while failing 'sustainability' standards indicates that the school is trending towards financial distress.

Each measure has up to two classifications that indicate risk: 'does not meet standard' or 'falls far below standard.' However, no single response that indicates risk is a standalone 'red flag' or a hard trigger for action. When a target is missed, the first response should be to understand the underlying reason. Authorizers should first consult the board to understand the narrative. In many cases, flagged events may have been planned, such as the building of a facility or accruing expenses at the end of the school year. A holistic look at the school should ultimately guide the level of concern. If a school has two or more ratings of 'does not meet standard' or one or more of 'falls far below standard,' authorizers should request more information, such as year-to-date financial statements, year-to-date budget variance reports, and updated budget projections. To highlight when there is the need for follow-up or more serious intervention, some authorizers have adapted this framework to a three-tiered system* (assigning schools a red, yellow, and green rating).

1. Near-term Measures

A. CURRENT RATIO: <i>Current assets divided by current liabilities</i>
<input type="checkbox"/> Does not meet standard: Less than or equal to 1.0 or between 1.0 and 1.1 with negative one-year trend. <input type="checkbox"/> Falls far below standard: Less than or equal to 0.9.
B. UNRESTRICTED DAYS CASH: <i>Unrestricted cash divided by ((Total expenses minus depreciation expense)/365)</i>
<input type="checkbox"/> Does not meet standard: Between 15-30 days or between 30-60 days with negative one-year trend. <input type="checkbox"/> Falls far below standard: Fewer than 15 days.

* For example, the New Mexico Public Education Commission and the Delaware Department of Education adopted the 'green', 'yellow', and 'red' rating system mapped to the NACSA categories.

C. ENROLLMENT VARIANCE: <i>Actual enrollment divided by enrollment projection</i>
<input type="checkbox"/> Does not meet standard: Between 85-95% in the most recent year. <input type="checkbox"/> Falls far below standard: Less than 85% in the most recent year.
D. DEFAULT
<input type="checkbox"/> Falls far below standard: School is in default or delinquent on debt service payments.

2. Sustainability Measures

A. TOTAL MARGIN AND AGGREGATED TOTAL MARGIN Total Margin: <i>Net income divided by total revenue</i> Aggregated Total Margin: <i>Total three-year net income divided by total three-year revenue</i>
<input type="checkbox"/> Does not meet standard: Aggregated three-year total margin greater than -1.5%, but trend is negative for last two years. <input type="checkbox"/> Falls far below standard: Aggregated three-year total margin is less than or equal to -1.5%, or most recent year total margin is less than -10%.
B. DEBT TO ASSET RATIO: <i>Total liabilities divided by total assets</i>
<input type="checkbox"/> Does not meet standard: Between 0.9 and 1.0. <input type="checkbox"/> Falls far below standard: Greater than 1.0.
C. CASH FLOW
<input type="checkbox"/> Does not meet standard: Multi-year cumulative cash flow is positive, but trend is negative. <input type="checkbox"/> Falls far below standard: Multi-year cumulative cash flow is negative.
D. DEBT SERVICE COVERAGE RATIO: <i>(Net income + Depreciation + Interest expense)/(Annual principal, interest, and lease payments)</i>
<input type="checkbox"/> Does not meet standard: Less than 1.1.

3. Additional Non-NACSA Measures

OTHER WARNING SIGNS¹⁴
<input type="checkbox"/> <i>Significant variation in actuals to budgeted figures.</i> May indicate that budget projections are not realistic, or there are significant changes in the environment. Ensure that forward estimates are adjusted accordingly.
<input type="checkbox"/> <i>Constant accounts receivable throughout the year.</i> Constant accounts receivables indicate that the school is not collecting invoiced amounts properly.
<input type="checkbox"/> <i>Constant or increasing accounts payable.</i> Constant accounts payable indicates that the school is not making payments as requested.
<input type="checkbox"/> <i>Constant or steadily increasing payroll taxes and retirement balances.</i>

Constant or steadily increasing payroll taxes and retirement balances may indicate that the school is not making the appropriate contributions.

- ☐ *Significantly higher expenses than district average or similar institutions (e.g. per pupil, per pupil occupancy, and instructional expense).*

- ☐ *Qualified opinions on the financial audit.*

Any qualified opinions from the auditor indicate that the information was limited in scope or did not meet Generally Accepted Accounting Principles (GAAP).

- ☐ *Presence of short-term or bridge loans to cover shortfalls from cash flow constraints.*

Management

Authorizers must ensure that the school properly addresses any issues in a timely and effective manner. While specific actions vary according to the issue, the checklist below outlines important considerations. Year-end deficits and insufficient funds are immediate problems, but financial problems often point to a greater underlying issue that may require fundamental changes.

1. DETERMINE THE SEVERITY OF THE PROBLEM

- ☐ *Review 'high-priority' schools.*

As part of the intervention policy, conduct a comprehensive follow-up review of schools that are flagged as 'high-priority' and clearly communicate with schools. Request additional documentation, including:¹⁵

- Year-to-date unaudited financial statements;
- Year-to-date budget variance reports; and
- Updated budget projections.

Authorizers should conduct board interviews to understand the narrative behind negative financial trends, triggers, and underlying vulnerabilities.

2. CREATE A STRATEGY TO ADDRESS ISSUES

- ☐ *Determine appropriate corrective actions.*

The authorizer should increase monitoring and the frequency of check-ins as the level of concern increases. While financial performance is the most prevalent reason for closure, if a school is performing academically but does not meet all standards for financial performance, the authorizer may decide to allow the school to continue operating and monitor it closely.¹⁶

3. ADDITIONAL CONTROLS

- ☐ *Ensure implementation of appropriate financial controls.*

Authorizers should confirm the creation and practice of proper financial controls.



TOOLBOX: *Financial Health and Sustainability*

- DC Public Charter School Board (DC PCSB): [Best Practices and Resources](#)
A compilation of sample reports that DC PCSB uses to practice effective oversight including a sample financial audit review report.
- Colorado League of Charter Schools: [Authorizer Tools and Resources](#)
These tools to improve authorizer practice offer several sample resources including an authorizer feedback tool, board governance training, and a school quality framework.
- National Charter School Resource Center (NCSRC): [Financial Performance Analysis and Monitoring Webinar](#)
This webinar features NACSA presenters discussing the role of the NACSA Core Performance Framework in monitoring school financial health.
- Fiscal Crisis and Management Assistance Team (FCMAT): [Charter School Annual Oversight Checklist](#)
FCMAT presents an updated version of a checklist for authorizers to use in their oversight activities. Each checklist includes best practices to help schools improve their operations and oversight.

FINANCIAL OVERSIGHT: FRAUD AND MISFEASANCE



Prevention

Both charter schools and those who oversee them have responsibilities to prevent fraud. Schools need to have strong practices in place and ensure that they are uniformly carried out. Authorizers must be aware of what strong financial practices look like and ensure that the schools they oversee implement appropriate controls and practices. Policies should clarify each party's responsibilities, and include provisions that stipulate that authorizers and other appropriate state entities have the authority to intervene if necessary. State law can affect the oversight authority of various entities. Authorizers should ensure that each policy is in place and carried out with fidelity.

1. CHECK FOR A CULTURE OF FISCAL ACCOUNTABILITY

- ☐ *Review the financial policies and procedures manual and written code of fiscal conduct, which should be shared with all employees.*

2. ENSURE TRANSPARENCY AND ACCOUNTABILITY

- ☐ *Assess the strength of internal controls.*
Authorizers should ensure that applications for new schools they approve include clear, sufficient plans for a fiscal structure designed with appropriate controls and practices such as those described in this section. Authorizers can require operating schools to inform and update the authorizer on their financial policies and practices as they evolve. Authorizers may also establish standard fiscal policies that they require of all schools for which they have oversight responsibilities.
- ☐ *Confirm multiple layers of accountability in the reporting structure.*
There should be multiple layers of financial oversight. The authorizer should take into account that the complexity of a school's staff may vary, but every school can adopt different layers of oversight.
- ☐ *Check for the separation of duties.*
No single individual should have control over two or more phases of a financial transaction or business operation.
- ☐ *Verify there is a checks and balances policy.*

Multiple signatures should be required for all checks and disbursements over a determined threshold and every authorization of payment.
3. ENSURE PROPER PROCUREMENT AND CONTRACTING
<input type="checkbox"/> <i>Review evidence of and compliance with conflict of interest policies.</i> Authorizers should ensure decision-making is free of conflicts of interest and regularly require the disclosure of potential or perceived conflicts of interest. Ideally, disclosures should be given annually but may depend on state law.
4. CHECK FOR RESTRICTIONS ON ACCESS TO FUNDS
The authorizer should ensure that the following policies are in place to protect the access to funds: <ul style="list-style-type: none"> <input type="checkbox"/> <i>A credit card policy.</i> Credit cards usage should be limited to a select number of staff members. <input type="checkbox"/> <i>A fund disbursement policy.</i> Authority to expend funds on behalf of the school should be limited to a few individuals, each of whom should be thoroughly vetted and subject to transparency and accountability requirements. <input type="checkbox"/> <i>A policy for cash receipt and disbursement.</i> <input type="checkbox"/> <i>A reimbursement policy.</i> Reimbursement of expenses should be prudential, transparent, and subject to the school's standard financial practices.
5. INSPECT HUMAN RESOURCES
<input type="checkbox"/> <i>Review salary schedule of highly-compensated employees.</i> Ensure the salary structure aligns with industry standards and is not excessive when compared to other charter schools. If salaries are higher, the authorizer can request reasons for variance, as charter school salaries may differ from those in traditional public schools for legitimate reasons.
6. REVIEW AND MAINTAIN ACCURATE RECORDS AND ACCOUNTS
<input type="checkbox"/> <i>Understand accounting standards.</i> Schools and authorizers should be fully familiar with statewide accounting standards (e.g. Financial Accounting Standards Board in New York, the more restrictive Government Accounting Standards Board in New Jersey, and the still more restrictive controls in Hawaii that regulate charter schools as governmental entities).
7. ENSURE PROPER EXTERNAL AUDITS
<input type="checkbox"/> <i>Require all charter schools to submit to an independent annual financial audit.</i> Authorizers should document the scope of audit requirements so that the financial audits have all information necessary to make an evaluation of the school's financial management.
8. CHECK OVERSIGHT CAPACITY
<input type="checkbox"/> <i>Define authorizer oversight role.</i> Authorizers should incorporate their system for oversight and intervention into charter contracts. Authorizers should check state law and policies to determine their oversight role in the charter contracts they administer as well as the ability to act when necessary.

☐ *Clarify authorizer protocol and policies.*

Authorizers should make clear that there are consequences for violations of acceptable practices and policies and how the escalation of consequences functions.

Identification

Despite the variety of fraud cases, instances of financial fraud in charter schools have consistent themes of inadequate internal controls, lax practices, and insufficient oversight at the management, board, and authorizer levels. We have included the most prevalent areas of weakness as common indicators of concern below.¹⁷ While the presence of these indicators does not confirm fraud, the presence of one or more requires further investigation. Any authorizer actions related to the investigation of fraud may be subject to public scrutiny under the Freedom of Information Law or become publicly available in other ways (e.g., report of authorizer findings, notification of school probation, etc.). To fulfill oversight responsibilities, authorizers must be diligent in identifying and investigating any suspicious activity.

1. COMMON WARNING SIGNS IN FINANCIAL RECORDS

- ☐ *Unusual and unexplained drops in profit or cash reserves.*
- ☐ *Lack of original receipts for reimbursement of expenses.*
- ☐ *Missing and disorganized documentation, such as vendor contracts.*
- ☐ *Large and unexplained increases in payments, management fees, or salaries.*

2. COMMON WARNING SIGNS IN FISCAL PRACTICES

- ☐ *Concentration of authority.*
Financial practices that concentrate too much authority in a single person, rather than layers of responsibility (e.g., the person who incurred the expense signs off on approval for payment).
- ☐ *Little to no transparency.*
- ☐ *An unqualified individual managing the school's finances.*
- ☐ *Lack of implementation of written financial policies.*
- ☐ *Weak checks and balances policies.*
Weak policies include caps on staff authority to sign checks that are set too high or not at all (e.g., no additional signatories required for large checks).
- ☐ *Unresponsive board.*
Some examples of this may be that the school's board or its finance committee is not attentive to budgets, audits, problems as they arise, or to general oversight of fiscal matters.

Management

The authorizer has a duty to conduct a fair and thorough investigation of any evidence of fraud. Below are several recommendations, organized by phases, for authorizers responding to potential fraud or misfeasance.

1. INITIAL ALLEGATION OR SUSPICION
<p><input type="checkbox"/> <i>Clearly document and carefully maintain records of all actions and decisions.</i> Documentation ensures that the oversight bodies have fulfilled all of their responsibilities and can support any future investigations.</p> <p><input type="checkbox"/> <i>Designate the appropriate body to investigate.</i> Some questions to ask include:</p> <ul style="list-style-type: none"> ○ Should the authorizer or some other state or district entity investigate? ○ Is there a special investigative unit that handles such issues? ○ If the authorizer has the authority to investigate, does it have the bandwidth to handle an investigation itself? ○ Should it engage an outside investigator? <p>The authorizer can also require the school to engage an independent fiscal expert to confirm whether or not finances were being represented fairly. In that scenario, the authorizer should clarify who is expected to bear that expense.</p>
2. INVESTIGATION
<p><input type="checkbox"/> <i>Interview individuals in the school and take notes on their statements.</i></p> <p><input type="checkbox"/> <i>Gather information about financial practices.</i></p> <p><input type="checkbox"/> <i>Look for discrepancies.</i> Attempt to understand and reconcile any disparities among records and materials (e.g., receipts, purchase orders, coding of expenses, accounts, financial statements, related party transactions). Review audited financials, compare them to self-reported statements and accounts, and focus particularly on auditor notes and, where relevant, third-party transactions.</p> <p><input type="checkbox"/> <i>Escalate if necessary.</i> If the authorizer uncovers significant irregularities, the next step is to determine if a crime has been committed. If so, the authorizer should inform law enforcement. To the extent that applicable law requires the authorizer to share its findings with other governmental entities, it should do so.</p>
3. INTERVENTION AND CORRECTIVE ACTION
<p><input type="checkbox"/> <i>Determine appropriate interventions.</i> Consequences for violations of acceptable practices and policies (e.g. probation, corrective plans, or charter non-renewal or revocation) should be clear to the authorizer and the schools it oversees in advance of any particular investigation.</p> <p><input type="checkbox"/> <i>Consider timing implications.</i></p>

Investigators need to consider how any investigation may impact upcoming high-stakes decisions, such as charter renewal or revocation. It is also necessary to consider the impact on students, with a particular emphasis on avoiding school closure during the academic year.

☐ *Communicate clearly with the school.*

Whether or not there are indicators of misfeasance, the authorizer should identify each area of concern and communicate with the school in writing about the investigator's findings. Early identification of mismanagement or impropriety is important, and the authorizer should address any concerns in periodic reviews.

☐ *Determine appropriate corrective action.*

Small to moderate-sized problems may be subject to a corrective plan, through which the authorizer holds the school accountable for remedying deficiencies in a specified period or face consequences such as closure or non-renewal. More serious problems could lead the authorizer to revoke the school's charter. Short of revocation, the authorizer might impose other corrective actions such as additional reporting requirements, engagement of a different auditor or other similar steps. Charter contracts and authorizer policies should specify the authority of the authorizer to impose such requirements on all charter schools under its supervision.



TOOLBOX: *Fraud and Misfeasance*

Additional information for boards and authorizers on fraud and mismanagement:

- NACSA: [Core Organizational Performance Framework Guidance](#)
While the financial framework helps identify issues with financial results, the 'financial management' section of the organizational performance framework pertains to internal processes including internal controls and governance of charter schools.
- Association of Certified Fraud Examiners: [Managing the Business Risk of Fraud](#) and [Sample Fraud Policy](#)
While not specific to the charter sector, this document contains key considerations and recommendations for internal fraud.
- Council of Nonprofits: [Internal Controls for Nonprofits](#)
This site offers multiple resources applicable to all charter schools, for creating responsible internal controls to prevent fraud and mismanagement.
- American Institute of Certified Public Accountants: [Sample Whistleblower Policy](#)
This document provides a sample whistleblower policy, but it should be amended to pertinent state laws.

FINANCIAL OVERSIGHT: FRAUD AND MISFEASANCE



New Schools

New schools are the most financially vulnerable. The greatest potential issues are similar to those of established schools: facilities and enrollment. However, due to the absence of previous information on enrollment and expenses, as well as constrained cash flows, external risks are of greater concern. Research shows that ineffective schools may demonstrate financial issues in the first few years before showing any indication of poor academic performance.¹⁸ Financial vulnerability may stem from early-stage failure to attract sufficient enrollment and a lag in performance data. While there may be schools with financial issues that are high-performing academically, severe financial issues ultimately impact all areas of performance.

ROLE OF THE AUTHORIZER

- ☐ *Require a solid business plan and effective governance and management systems.*
A business plan should include details of how the school will be managed, a market analysis, and information on how students will be served and recruited.
- ☐ *Ensure financial expertise in management through interviews and statements of interest at the application stage.*
Authorizers should screen the resumes of proposed board members for financial, real estate, and fundraising skills, among other competencies. In-depth interviews of the founding board can support documentation.
- ☐ *Ensure that the charter contract sets attainable and realistic financial goals.*

Management Companies

Authorizers must preserve the ability to exercise complete oversight over how school funds are used. Most educational service providers are structured as nonprofit organizations, also called charter management organizations (CMOs), while others are for-profit, or education management organizations (EMOs). Management

companies can provide either selective services or comprehensive management. The scope can include educational and administrative services, including accounting, procurement, and reporting.¹⁹ Authorizers should look for evidence of a clear performance-based relationship.

REVIEWING THE MANAGEMENT AGREEMENT

- ☐ *Ensure independent board fiscal oversight.*
Look for the assignment and allowance of full board fiscal oversight in the management agreement. The agreement should not exclude the board from access to financial documentation and authority over the budget.
- ☐ *Make sure that board has independent and necessary support.*
Authorizers should ensure that boards independently select, retain, and compensate a school attorney, accountant, and audit firm.
- ☐ *Review and approve all third party management agreements.*
Ensure the primacy of the charter contract over the management agreement.
- ☐ *Ensure that the board retains financial control.*
Ensure funds, at least initially, go into an account controlled by the board and not by the management company. If one of the functions of the management company is to pay school bills, the school funds may be diverted into an account controlled by the management company from the school bank account. The school should pay the management company from an account that is controlled by the board and has restricted access..
- ☐ *Require disclosure of loans and investments.*
Authorizers should require disclosure and documentation of any loans or investments by the contracted party to the school.



TOOLBOX: Management Companies

- **NACSA: [A Toolkit for Working with Education Service Providers](#)**
This toolkit includes materials developed by authorizers to help charter schools work with education service providers.

CONCLUSION



While this toolkit targets authorizers, fiscal oversight is important for all charter school stakeholders. In implementing the recommendations above, it is important for authorizers to partner with charter school boards in exercising oversight to ensure clear communication and a holistic understanding of the school's practices. Authorizers must also be careful to respect the school's autonomy in matters such as budgeting and planning. The best way to prevent financial issues is to ensure that the school has the proper fiscal and internal controls from the initial application phase. Authorizer practices can vary substantially across states in the management of financial issues. Not all state policies assign clear lines of authority for investigations or to enforce corrective actions; there may also be ambiguity over control of non-renewal and revocation decisions based on inappropriate behavior. that the power for authorizers to act on these matters must exist, even in situations where a charter school's academic results are acceptable. When this level of authorizer oversight exists, charter schools as a whole can better serve the public to whom they are ultimately accountable.

Quick Reference Guide

AUTHORIZER FISCAL OVERSIGHT <i>Full fiscal oversight must consider both the general financial health of the school and the risk of fraud.</i>	
Financial Health and Sustainability <i>Effective financial management to avoid default</i>	Fraud and Mifeseance <i>Good governance to mitigate fraud risk</i>
<p style="text-align: center;"><u>Prevent</u></p> <ul style="list-style-type: none"> ✓ Ensure sufficient financial literacy, both with board and the authorizer. ✓ Approve a conservative budget and forecasts, checking the budget, underlying budget assumptions, and the long-term financial plan. ✓ Establish regular and consistent authorizer monitoring practices appropriate to the risk-level of the school, ensuring that the board also has regular financial reviews. 	<p style="text-align: center;"><u>Prevent</u></p> <ul style="list-style-type: none"> ✓ Check for transparency and accountability in the school's practices and procedures through the presence of proper internal controls. ✓ Ensure that all procurement and contracting is free of all conflicts of interest. ✓ Understand statewide accounting standards to make sure that the school is maintaining accurate records and accounts. ✓ Require an independent annual financial audit for all schools. ✓ Define and communicate authorizer oversight role and clarify escalation path of consequences.
<p style="text-align: center;"><u>Identify</u></p> <ul style="list-style-type: none"> ✓ Use a rubric to assess the immediate and longer-term financial state of the school, such as the NACSA Core Performance Framework. ✓ Scan for other warning signs, such as large variations between budgets and actuals, significantly high expenses, qualified audit opinions, and bridge loans. 	<p style="text-align: center;"><u>Identify</u></p> <ul style="list-style-type: none"> ✓ Look for warning signs in financial records, such as sudden drops in profit or cash, no receipts, missing documentation, and large increases in payments or salaries. ✓ Look for warning signs in a school's fiscal practices, such as the concentration of authority, no transparency, unqualified financial management, no implementation of policies, weak checks and balances, and an unresponsive board.
<p style="text-align: center;"><u>Manage</u></p> <ul style="list-style-type: none"> ✓ If a school fails to meet standards, conduct a follow-up analysis to determine the severity 	<p style="text-align: center;"><u>Manage</u></p> <ul style="list-style-type: none"> ✓ Upon initial suspicion, clearly document all decisions and designate the appropriate investigative body.

<p>of financial issues by reviewing all 'high-priority' schools.</p> <ul style="list-style-type: none">✓ Carefully determine the appropriate corrective actions for the school after fully understanding the situation.	<ul style="list-style-type: none">✓ Conduct thorough investigation to understand whether the issue should be escalated or a crime has been committed.✓ Intervene where necessary but being careful to minimize impacts on students.
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Appendix A: Detailed NACSA Financial Performance Framework

1. Near-term Measures

	Meets	Does not Meet	Far Below
A. Current Ratio <i>Current assets divided by current liabilities</i>	<input type="checkbox"/> Greater than or equal to 1.1; <i>or</i> <input type="checkbox"/> Between 1.0 and 1.1 and positive one-year trend.	<input type="checkbox"/> Between 0.9 and 1.0 or equal to 1.0; <i>or</i> <input type="checkbox"/> Between 1.0 and 1.1 with negative one-year trend.	<input type="checkbox"/> Less than or equal to 0.9.
B. Unrestricted Days Cash <i>Unrestricted cash divided by ([Total expenses minus depreciation expense]/365)</i>	<input type="checkbox"/> 60 days cash; <i>or</i> <input type="checkbox"/> Between 30 and 60 days cash and one-year trend is positive.	<input type="checkbox"/> Between 15-30 days cash; <i>or</i> <input type="checkbox"/> Between 30 and 60 days cash and one-year trend is negative.	<input type="checkbox"/> Fewer than 15 days cash.
C. Enrollment Variance <i>Actual enrollment divided by enrollment projection</i>	<input type="checkbox"/> Equals or exceeds 95% in most recent year.	<input type="checkbox"/> Between 85-95% in the most recent year.	<input type="checkbox"/> Less than 85% in the most recent year.
D. Default	<input type="checkbox"/> Not in default of loan and/or not delinquent with debt payments.	Not applicable	<input type="checkbox"/> In default of loan and/or delinquent with debt service payments.

2. Sustainability Measures

	Meets	Does not Meet	Far Below
A. Total Margin <i>Net income divided by total revenue</i> Aggregated Total Margin <i>Total three-year net income divided by total three-year revenue</i>	<input type="checkbox"/> Aggregated three-year total margin is positive and most recent year total margin is positive; <i>or</i> <input type="checkbox"/> Aggregated three-year total margin is greater than -1.5%, trend is positive for last two years, and the most recent year total margin is positive.	<input type="checkbox"/> Aggregated three-year total margin is greater than -1.5%, but trend does not meet standard.	<input type="checkbox"/> Aggregated three-year total margin is less than or equal to -1.5%; <i>or</i> <input type="checkbox"/> Most recent year total margin is less than -10%.
B. Debt to Asset Ratio <i>Total liabilities divided by total assets</i>	<input type="checkbox"/> Less than 0.9.	<input type="checkbox"/> Between 0.9 and 1.0.	<input type="checkbox"/> Greater than 1.0.
C. Cash Flow <i>Multi-year cash flow</i> <i>One-year cash flow</i>	<input type="checkbox"/> Multi-year cash flow is positive and one-year cash flow is positive each year; <i>or</i> <input type="checkbox"/> Multi-year cash flow is positive, cash flow positive in one of two years, and cash flow in most recent year positive.	<input type="checkbox"/> Multi-year cash flow positive, but trend does not 'meet standard'.	<input type="checkbox"/> Multi-year cash flow is negative.
D. Debt Service Coverage Ratio <i>(Net income + Depreciation + Interest Expense)/(Annual principal,</i>	<input type="checkbox"/> Equal or exceeds 1.1.	<input type="checkbox"/> Less than 1.1.	Not applicable

<i>interest, and lease payments)</i>			
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